

**TENNESSEE DEPARTMENT OF REVENUE  
LETTER RULING # 07-08**

**WARNING**

**Letter rulings are binding on the Department only with respect to the individual taxpayer being addressed in the ruling. This presentation of the ruling in a redacted form is informational only. Rulings are made in response to particular facts presented and are not intended necessarily as statements of Department policy.**

**SUBJECT**

Statutory requirements to qualify for incentives available for the production of a movie in Tennessee.

**SCOPE**

This letter ruling is an interpretation and application of the tax law as it relates to a specific set of existing facts furnished to the Department by the taxpayer. The rulings herein are binding upon the Department, and are applicable only to the individual taxpayer being addressed.

This letter ruling may be revoked or modified by the Commissioner at any time. Such revocation or modification shall be effective retroactively unless the following conditions are met, in which case the revocation shall be prospective only:

- (A) The taxpayer must not have misstated or omitted material facts involved in the transaction;
- (B) Facts that develop later must not be materially different from the facts upon which the ruling was based;
- (C) The applicable law must not have been changed or amended;
- (D) The ruling must have been issued originally with respect to a prospective or proposed transaction; and
- (E) The taxpayer directly involved must have acted in good faith in relying upon the ruling and a retroactive revocation of the ruling must inure to his detriment.

## **FACTS**

[THE TAXPAYER] is a yet-to-be formed Tennessee limited liability company. It will be owned by two individuals, [INDIVIDUAL NAMES] (the “Producers”), both of whom currently reside in [CITY OUTSIDE TENNESSEE] where they produce a wide variety of movies, both in and out of the [STATE WHERE THE PRODUCERS RESIDE]. The Producers will form [THE TAXPAYER] in Tennessee and move their production work to Tennessee.

Each of the producers is currently in the process of purchasing a home in Tennessee and they plan to move to Tennessee during the coming months. Upon their relocation in Tennessee and the formation of [THE TAXPAYER], the Producers will permanently reside in Tennessee and will be domiciled in Tennessee. Although the Producers will continue to have some production work outside Tennessee, the majority of their production work will be in the State of Tennessee.

[THE TAXPAYER’S] headquarters and principal office will be in the State of Tennessee and will probably be located in the [TENNESSEE CITIES] area. The Producers and any other headquarters staff will be employed and located in this office and [THE TAXPAYER’S] primary headquarters related functions and services will be performed there. [THE TAXPAYER] will not produce any movies that 18 U.S.C. § 2257 requires records to be maintained with respect to any performer portrayed in the movie.<sup>1</sup>

## **QUESTIONS PRESENTED**

1. Will the formation of [THE TAXPAYER] as a Tennessee limited liability company, the establishment of its principal office and headquarters in the State of Tennessee and the Producer’s relocation to the State of Tennessee qualify as establishing a “headquarters facility,” Pursuant to Tenn. Code Ann. § 67-6-224(b)(3) and for purposes of Tenn. Code Ann. § 67-4-2109(k)(2)?
2. Will the costs and expenses incurred by [THE TAXPAYER] in Tennessee to produce movies in the State of Tennessee be deemed to be “qualified expenses,” as defined in Tenn. Code Ann. § 67-4-2109(k)(1)(A)?
3. If [THE TAXPAYER] incurs at least \$1,000,000 in “qualified expenses”, will it be deemed a “qualified production company,” as the term is defined in Tenn. Code Ann. § 67-4-2109(k)(1)(C)?
4. Assuming that each of the above questions are answered in the affirmative, will

---

<sup>1</sup> The facts stated in this paragraph were confirmed by [THE TAXPAYER’S ATTORNEY] in a March 15, 2007 telephone conversation with a representative of the Tennessee Department of Revenue. Title 18 U.S.C. § 2257 pertains to record keeping requirements for the producer of a film that contains one or more visual depictions made after November 1, 1990 of actual sexually explicit conduct.

[THE TAXPAYER] be entitled to the refund for qualified expenses as set forth in Tenn. Code Ann. § 67-4-2109(k)(2)?

5. Tenn. Code Ann. § 67-4-2109(k)(1)(C) states that to be deemed a “qualified production company,” an entity must incur at least \$1,000,000 in “qualified expenses.” Is this a one-time threshold requirement?
6. Tenn. Code Ann. § 67-4-2109(k)(1)(A) states that “qualified expenses” are those expenses incurred in Tennessee that “are necessary for the production of a movie in Tennessee that is in the best interests of the state.”
  - (a) What does the language “necessary for the production of a movie in Tennessee” mean?
  - (b) What does the language “in the best interests of this state” mean?
7. What documentation is required to evidence “qualified expenses”?

### **RULINGS**

1. Yes.
2. Yes, provided that the costs and expenses are determined by the Commissioner of Revenue and the Commissioner of Economic and Community Development to be necessary for the production of a movie in Tennessee that is in the best interests of the State of Tennessee.
3. Yes.
4. Yes, provided that all applicable statutory requirements of Tenn. Code Ann. § 67-4-2109(k) are met.
5. No. The qualified production company must incur at least \$1,000,000 in qualified expenses for the production of each movie produced in Tennessee that is eligible for the incentive refund.
6. (a) Expenses “necessary for the production of a movie in Tennessee” are expenses incurred in Tennessee without which the movie could not have reasonably been made. The phrase “necessary for the production of a movie in Tennessee” does not mean only the expenses that would be necessary to make the movie in Tennessee on the lowest possible budget.
  - (b) A movie that contains one or more visual depictions of actual sexually explicit conduct, or a movie that, in the opinion of the Commissioner of Revenue and the Commissioner of Economic and Community Development, would bring disgrace, infamy, reproach or stigma to the State of Tennessee in the eyes of the general

public because of its subject matter or visual depictions, would not be “in the best interests of this state” and its producer will not be rewarded by the incentives provided in Tenn. Code Ann. § 67-4-2109(k) for making the movie in Tennessee.

7. Any documentation that, in the opinion of the Commissioner, is necessary to satisfy him that the expenses claimed are eligible for the statutory incentive will be required. Actual documentation required will be determined by the Commissioner on a case-by-case basis and may vary depending on the factual situation with which the Commissioner is presented.

The minimal documentation in every case will be a listing of the expenses incurred and the name and address of each vendor to whom each expense was paid. In any case, the Commissioner will not require any more documentation regarding “qualified expenses” than is absolutely and reasonably necessary to satisfy him that the expenses claimed are eligible for the statutory incentive.

## **ANALYSIS**

### **APPLICABLE STATUTES**

The following definitions are set forth in Tenn. Code Ann. § 67-4-2109(k)(1) with regard to the availability of a refund for a percentage of the expenses incurred in producing a movie in Tennessee:

- (A) “Qualified expenses” means those expenses incurred in Tennessee that both the commissioner of revenue and the commissioner of economic and community development determine, in their sole discretion, are necessary for the production of a movie in Tennessee that is in the best interests of this state. For purposes of this subdivision (k)(1)(A), “best interests of this state” includes, but is not limited to, a determination that production of the movie does not require that records be maintained pursuant to 18 U.S.C. § 2257 with respect to any performer portrayed in the movie.
- (B) “Qualified investor” means any entity that has established a headquarters facility as defined in § 67-6-224 that has invested in a qualified production company; and
- (C) “Qualified production company” means any entity that incurs at least one million dollars (\$1,000,000) in qualified expenses.

Tenn. Code Ann. § 67-6-224(b)(3), referenced in Tenn. Code Ann. § 67-4-2109(k)(1)((B) above, defines a “headquarters facility” as follows:

- (3) “Headquarters facility” means a facility in this state that houses the international, national, or regional headquarters of a taxpayer, where headquarters staff employees are located and employed, and where the primary headquarters

related functions and services are performed.

Tenn. Code Ann. § 67-4-2109(k) makes the following provisions for a qualified production company or a qualified investor that has established a headquarters facility in Tennessee to obtain a refund of a percentage of the expenses incurred in producing a movie in Tennessee:

- (2) A refund in an amount equal to fifteen percent (15%) of any qualified expenses shall be allowed to any qualified production company that has established a headquarters facility as defined in § 67-6-224. If the qualified production company does not have a headquarters facility as defined in § 67-6-224, then any qualified investor shall be allowed a refund equal to the amount of refund that the qualified production company would have been entitled to had it established a headquarters facility as defined in § 67-6-224, multiplied by the qualified investor's percentage ownership interest in the qualified production company.
- (3) In order for either a qualified production company or a qualified investor to become entitled to a refund, the qualified production company must submit documentation verifying the qualified expenses.
- (4) The commissioner shall review the documentation and notify the qualified production company of the approved amount.
- (5) Once the qualified production company has been notified of the approved amount, either the qualified production company or the qualified investment company, as appropriate, may submit a claim for refund. The refund shall be subject to the procedures of § 67-1-1802; provided, however; notwithstanding any procedure of § 67-1-1802 to the contrary, that a claim for refund shall be filed with the commissioner within three (3) years from December 31 of the year in which the qualified expenses were incurred. In no case shall a refund for the same qualified expenses be allowed twice.

#### APPLICATION OF THE STATUTES TO A QUALIFIED PRODUCTION COMPANY

The statutes set forth above provide that a "qualified production company" that produces a movie in Tennessee may qualify for a refund of 15% of the "qualified expenses" of producing the movie if the following requirements are met:

1. A "qualified production company" must be established in Tennessee that:
  - (a) Is a "headquarters facility" that houses the entity's international, national, or regional headquarters; and

- (b) Is the employment location and physical location of the entity's headquarters staff employees; and
  - (c) Is where the entity's primary headquarters related functions and services are performed.
- 2. The entity so established must:
  - (a) Incur at least \$1 million in Tennessee "qualified expenses" in the production of a movie in Tennessee; and
  - (b) Secure a written determination by the Commissioner of Revenue and the Commissioner of Economic and Community Development stating that:
    - (i) The movie is in the best interest of Tennessee; and
    - (ii) The expenses incurred in producing the movie were necessary for the production of the movie in Tennessee; and
    - (iii) The movie does not contain 1 or more visual depictions, made after November 1, 1990, of actual sexually explicit conduct. (See 18 U.S.C. § 2257)
- 3. The "qualified production company" must submit documentation of the expenses incurred in producing the movie to the Commissioner of Revenue.
- 4. Upon review of the documentation submitted for the expenses incurred in producing the movie, the Commissioner of Revenue must notify the "qualified production company" of the approved amount.
- 5. Within 3 years from December 31 of the year in which the expenses are incurred, the "qualified production company" must file a refund claim with the Department of Revenue for the expenses approved.
- 6. The refund claim must be processed under the provisions of Tennessee law which requires approval of the Commissioner of Revenue and the Tennessee Attorney General.
- 7. A qualified production company meeting the above outlined requirements will be refunded 15% of the "qualified expenses" that it incurs in the production of a movie in Tennessee.

We turn now to an analysis of the rulings made with regard to the questions presented.

1. [THE TAXPAYER] WILL BE CONSIDERED A “HEADQUARTERS FACILITY” UNDER THE PROVISIONS OF TENN. CODE ANN. § 67-6-224(b)(3) AND FOR PURPOSES OF TENN. CODE ANN § 67-4-2109(k)(2)

[THE TAXPAYER] will be considered a “headquarters facility” under the provisions of Tenn. Code Ann. §§ 67-6-224(b)(3) and for purposes of 67-4-2109(k)(2), if it:

1. Establishes a facility in Tennessee that houses its international, national, or regional headquarters; and
2. Its headquarters staff employees are located and employed at its Tennessee “headquarters facility”; and
3. Its primary headquarters related functions and services are performed at the facility.

The headquarters and principal office of [THE TAXPAYER] will be located in the State of Tennessee, probably in the [TENNESSEE CITIES] area. This is where the Producers and any other headquarters staff will be employed and located and [THE TAXPAYER’S] primary headquarters related functions and services will be performed there.

The facts presented clearly show that [THE TAXPAYER] will establish its headquarters at a facility in Tennessee where its headquarters staff employees will be located and employed and where its primary headquarters related functions and services will be performed. [THE TAXPAYER] will thus be considered a “headquarters facility” under the provisions of Tenn. Code Ann. § 67-6-224(b)(3) and for purposes of Tenn. Code Ann. § 67-4-2109(k)(2).

2. COSTS AND EXPENSES INCURRED BY [THE TAXPAYER] IN TENNESSEE TO PRODUCE A MOVIE IN THE STATE OF TENNESSEE WILL BE CONSIDERED “QUALIFIED EXPENSES” PROVIDED PROPER APPROVAL IS SECURED

Tenn. Code Ann. § 67-4-2109(k)(1)(A) defines “qualified expenses” for purposes of the incentives available for production of a movie in Tennessee. The statute sets forth the following criteria:

1. The expenses must be incurred in Tennessee to produce a movie in the State of Tennessee.
2. The Commissioner of Revenue and the Commissioner of Economic and Community Development must make a written determination stating that:
  - (a) The movie is in the best interest of Tennessee; and

(b) The expenses incurred were necessary for the production of the movie in Tennessee; and

3. The movie must not contain 1 or more visual depictions, made after November 1, 1990, of actual sexually explicit conduct. (See 18 U.S.C. § 2257)

Tenn. Code Ann. § 67-4-2109(k)(1)(C) requires the “qualified expenses” to be incurred by a “qualified production company” and requires that the expenses so incurred amount to at least \$1,000,000.

As explained in #3 below, [THE TAXPAYER] will be considered a “qualified production company” if it incurs “qualified expenses” of at least \$1,000,000 in Tennessee in the production of a movie in the State of Tennessee.

The facts presented state that [THE TAXPAYER] will not produce any movies that contain any visual depictions of actual sexually explicit conduct (See 18 U.S.C. § 2257). Upon securing a written determination from the Commissioner of Revenue and the Commissioner of Economic and Community Development stating that the costs and expenses incurred by [THE TAXPAYER] were necessary for the production of a movie in Tennessee that is in the best interests of the State of Tennessee, such costs and expenses will be deemed to be “qualified expenses,” as defined in Tenn. Code Ann. § 67-4-2109(k)(1)(A).

3. [THE TAXPAYER] WILL BE CONSIDERED A “QUALIFIED PRODUCTION COMPANY” IF IT INCURS “QUALIFIED EXPENSES” IN TENNESSEE OF AT LEAST \$1,000,000 IN THE PRODUCTION OF A MOVIE IN THE STATE OF TENNESSEE

In order to be considered a “qualified production company,” Tenn. Code Ann. § 67-4-2109(k)(1)(C) requires that the entity incur “qualified expenses” in Tennessee of at least \$1,000,000 to produce a movie in Tennessee.

If [THE TAXPAYER] incurs “qualified expenses” in Tennessee of at least \$1,000,000 in the production of a movie in the State of Tennessee, it will be considered a “qualified production company” for purposes of being eligible for incentives available under Tenn. Code Ann. § 67-4-2109(k) for production of a movie in Tennessee.

4. [THE TAXPAYER] WILL BE ENTITLED TO A REFUND OF 15% OF ITS “QUALIFIED EXPENSES” PROVIDED THAT IT MEETS ALL APPLICABLE STATUTORY REQUIREMENTS SET FORTH IN TENN. CODE ANN. § 67-4-2109(k)

In view of the facts presented and the rulings in response to questions 1 through 3 above, there is no reason to believe that [THE TAXPAYER] will not meet all of the applicable statutory requirements set forth in Tenn. Code Ann. § 67-4-2109(k) and



outlined in this Letter Ruling to qualify for a 15% refund of the qualified expenses that it incurs in the production of a movie in Tennessee.

5. THE “QUALIFIED EXPENSES” THRESHOLD OF \$1,000,000  
APPLIES TO EACH MOVIE PRODUCED  
BY A “QUALIFIED PRODUCTION COMPANY” IN TENNESSEE

Tenn. Code Ann. § 67-4-2109(k)(1)(C) states that a “qualified production company” is an “. . . entity that incurs at least \$1,000,000 in “qualified expenses.”

Tenn. Code Ann. § 67-4-2109(k)(1)(A) states that “qualified expenses” are “. . . those expenses incurred in Tennessee that . . . are necessary for the production of a movie in Tennessee . . .” (Emphasis underline added.)

According to these statutes, one of the requirements that a “qualified production company” must meet to be eligible for the movie production incentive refund provided by Tenn. Code Ann. § 67-4-2109(k)(2) is that the expenses that it incurs for the production of “a movie” in Tennessee must amount to at least \$1,000,000.

For example, suppose that expenses for the first movie that [THE TAXPAYER] produces in Tennessee amount to \$1,000,000. Assuming that all applicable statutory requirements are met, [THE TAXPAYER] will receive a refund of \$150,000 (15% of \$1,000,000).

For its second movie produced in Tennessee, suppose that [THE TAXPAYER] incurs expenses of \$990,000. [THE TAXPAYER] will not receive any refund because the \$1,000,000 “qualified expenses” threshold has not been met.

Assume expenses for the third movie produced by [THE TAXPAYER] in Tennessee amount to \$1,050,000 and all applicable statutory requirements are met. [THE TAXPAYER] will receive a refund of \$157,500 (15% of \$1,050,000).

6. (a) REQUIREMENT THAT “QUALIFIED EXPENSES”  
“ARE NECESSARY FOR THE PRODUCTION OF A MOVIE IN TENNESSEE”

Neither the term “necessary” nor any of the other terms in the phrase “. . . are necessary for the production of a movie in Tennessee . . .” found in Tenn. Code Ann. § 67-4-2109(k)(1)(A) are defined in the law.

The most basic rule of statutory construction is to ascertain and give effect to the intention and purpose of the legislature. *Worrall v. Kroger Co.*, 545 S.W.2d 736 (Tenn. 1977). Legislative intent or purpose is to be ascertained primarily from the natural and ordinary meaning of the language used, without forced or subtle construction that would limit or extend the meaning of the language. [\*National Gas Distributors, Inc. v. State\*, 804 S.W.2d 66 \(Tenn.1991\)](#). In seeking to determine the “natural and ordinary meaning” of statutory language, the usual and accepted source for such information is a

dictionary. *State v. Givens*, Slip op. 1994 WL406187 (Tenn.Crim.App. Aug. 4, 1994).

One of the definitions given for the word “necessary” in BLACK’S LAW DICTIONARY 928 (5<sup>th</sup> ed. 1979) is “. . . something which in the accomplishment of a given object cannot be dispensed with . . .” Among the definitions given for the word “necessary” in THE AMERICAN HERITAGE DICTIONARY 834 (2<sup>nd</sup> ed. 1982) are “[a]bsolutely essential; indispensable” and “[n]eeded to achieve a certain result . . .”

In view of the context of the phrase “. . . are necessary for the production of a movie in Tennessee . . .” and the definitions of the word “necessary” cited in the above paragraph, it appears that the legislative intent or propose is to classify expenses without which the movie could not have reasonably been made as a “qualified expenses.”

It does not appear that the legislature intended that only expenses that would be necessary to make the movie in Tennessee on the lowest possible budget will be allowed as “qualified expenses.”

It appears that the legislature only intended to give the Commissioner of Revenue and the Commissioner of Economic and Community Development the ability to review expenses that a “qualified production company” claims as “qualified expenses” to make sure that such expenses are reasonably related to the production of a movie in Tennessee.

For example, if a “qualified production company” had someone on its payroll that had nothing to do with making the movie in Tennessee, or who was merely present as a bystander when the movie was made, but did not actually do anything at any time in connection with the movie, then that person’s salary would not be allowed as a “qualified expense.” If a person in the employ of the “qualified production company” worked on many projects, including the making of a movie in Tennessee, then only the portion of such person’s salary paid while the person was actually working on making the particular movie in Tennessee would be allowed as a “qualified expense.” Expenses incurred outside Tennessee will not be allowed as “qualified expenses.”

6(b) MEANING OF THE LANGUAGE “IN THE BEST INTERESTS OF THIS STATE”  
IN TENN. CODE ANN. § 67-4-2109(k)(1)(A)

Tenn. Code Ann. § 67-4-2109(k)(1)(A) states that “qualified expenses” are limited to those expenses incurred in Tennessee that, in the sole discretion of the Commissioner of Revenue and the Commissioner of Economic and Community Development, are necessary for the production of a movie in Tennessee and “in the best interests of this state.”

By enactment of Tenn. Code Ann. § 67-4-2109(k), the Tennessee legislature obviously wants to encourage the making of movies in Tennessee. The legislature has provided an incentive to entities that choose to make movies in Tennessee and that meet the statutory requirements to qualify for the incentive offered. However, the legislature does

not want to encourage or reward the making of movies in Tennessee that are not “in the best interests of this state.”

The last sentence of Tenn. Code Ann. § 67-4-2109(k)(1)(A), set forth below, gives an example of a movie that would not be “in the best interests of this state:”

For purposes of this subdivision (k)(1)(A), “best interests of this state” includes, but is not limited to, a determination that production of the movie does not require that records be maintained pursuant to 18 U.S.C. § 2257 with respect to any performer portrayed in the movie.

Title 18 U.S.C. § 2257 is a federal law that pertains to record keeping requirements for the producer of a film that contains one or more visual depictions of actual sexually explicit conduct. The Tennessee legislature does not believe that the making of a movie in Tennessee that contains one or more visual depictions of actual sexually explicit conduct would be “in the best interests of this state” and does not want to reward entities who choose to make such movies in Tennessee.

A movie that, in the opinion of the Commissioner of Revenue and the Commissioner of Economic and Community Development, would bring disgrace, infamy, reproach or stigma to the State of Tennessee in the eyes of the general public because of its subject matter or visual depictions would not be “in the best interests of this state” and its producer would not be rewarded by the incentives provided in Tenn. Code Ann. § 67-4-2109(k) for making the movie in Tennessee.

## 7. DOCUMENTATION REQUIRED TO EVIDENCE “QUALIFIED EXPENSES”

Tenn. Code Ann. § 67-4-2109(k)(3) and (4) make the following provisions concerning the documentation of “qualified expenses” that are eligible for the statutory incentive for the making of a movie in Tennessee:

(3) In order for either a qualified production company or a qualified investor to become entitled to a refund, the qualified production company must submit documentation verifying the qualified expenses.

(4) The commissioner shall review the documentation and notify the qualified production company of the approved amount.

The statutes are so written that the Commissioner of Revenue may require any documentation that, in the opinion of the Commissioner, is necessary to satisfy him that the expenses are eligible for the statutory incentive. The actual documentation required will be determined by the Commissioner on a case-by-case basis and may vary depending on the factual situation with which the Commissioner is presented.

The minimal documentation in every case will be a listing of the expenses incurred and the name and address of each vendor to whom each expense was paid. If the nature of

the expense and its relationship to the movie produced is not obvious from such a listing, then a further explanation may need to be provided.

In some situations, the Commissioner may find it necessary to require a copy of the invoice evidencing each expense and/or a copy of the canceled check or other evidence of payment. Affidavits attesting to certain expenses, or certain work done in production of the movie in Tennessee could also be required in certain instances.

In any case, the Commissioner will not require any more documentation regarding "qualified expenses" than is absolutely and reasonably necessary to satisfy him that the expenses claimed are eligible for the statutory incentive.

\_\_\_\_\_  
Arnold B. Clapp  
Special Counsel to the Commissioner

**APPROVED:** \_\_\_\_\_  
Reagan Farr, Commissioner

**DATE:** 3-27-07